

FEDERAL RESERVE SYSTEM

12 CFR Parts 204

[Regulation D; Docket No. R-0988]

Reserve Requirements of Depository Institutions

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The Board is proposing amendments to Regulation D, Reserve Requirements of Depository Institutions, to move from the current system of contemporaneous reserve maintenance for institutions that are weekly reporters to a system under which reserves are maintained on a lagged basis by such institutions. Under a lagged reserve maintenance system, the reserve maintenance period for a weekly reporter will begin 30 days after the beginning of a reserve computation period. Under the current system, the reserve maintenance period begins only two days after the beginning of the computation period.

DATES: Comments must be submitted on or before January 12, 1997.

ADDRESSES: Comments, which should refer to Docket No. R-0988, may be mailed to Mr. William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. Comments addressed to Mr. Wiles also may be delivered to the Board's mail room between 8:45 a.m. and 5:15 p.m. and to the security control room outside of those hours. Both the mail room and the security control room are accessible from the courtyard entrance on 20th

Street between Constitution Avenue and C Street, N.W. Comments may be inspected in Room MP-500 between 9:00 a.m. and 5:00 p.m.

FOR FURTHER INFORMATION CONTACT: William Whitesell, Section Chief, Money and Reserves Projections Section, Division of Monetary Affairs (202/452-2967); Oliver Ireland, Associate General Counsel, (202/452-3625) or Lawranne Stewart, Senior Attorney (202/452-3513), Legal Division. For the hearing impaired only, contact Diane Jenkins, Telecommunications Device for the Deaf (TDD) (202/452-3544), Board of Governors of the Federal Reserve System, 20th and C Streets, N.W., Washington, D.C. 20551.

SUPPLEMENTARY INFORMATION:

In order to satisfy the reserve requirements imposed under Regulation D (Reserve Requirements of Depository Institutions), depository institutions that file detailed deposit reports with the Federal Reserve once a week ("weekly reporters") are required to maintain reserves against their deposits on a virtually contemporaneous basis.^{1/} Weekly reporters are required to maintain average reserve balances over a 14-day

^{1/} Weekly reporters include domestic depository institutions with total reservable liabilities greater than the exemption amount provided by the zero-reserve tranche, currently \$4.4 million, and total deposits at or above the deposit cut-off established for institutions that are not fully exempt from reserve requirements, currently \$75 million. U.S. branches and agencies of foreign banks and Edge and Agreement corporations, regardless of their size, must report weekly.

Institutions that are not weekly reporters file deposit reports on either a quarterly or annual basis, depending on the size of their total deposits and their total reservable liabilities. This proposal will have no effect on those institutions.

reserve maintenance period that begins only two days after the beginning of the 14-day computation period.^{2/} The requirement for contemporaneous reserve maintenance was implemented in 1984 to enhance the conduct of monetary policy by strengthening the ability of the Board to control M1, the narrowest measure of the money supply, through operations directed at the supply of reserves.^{3/}

Since that time, however, the Federal Reserve's operating procedures have changed and it no longer maintains target ranges for M1. Additionally, the use of contemporaneous reserve maintenance requires depositories and the Federal Reserve to estimate and project the quantity of reserves that will be needed to meet reserve requirements during the current maintenance period. These estimates have become increasingly difficult to formulate with any precision on a timely basis, in part because of the implementation by many depository institutions of retail sweep programs. Such programs have lowered required reserves for institutions that have implemented them and have increased uncertainties regarding the reserve balances depository institutions must hold at the Reserve Banks. For example, for some large institutions, required reserves are sometimes above and sometimes below their holdings of vault cash, with the result that it

^{2/} In the past, the threshold deposit level for weekly reporters has been indexed to the growth of total deposits and revised annually. As part of the Board's most recent review of the deposit reporting forms, however, the threshold deposit level for weekly reporting of deposits was raised to \$ 75 million, effective as of the reporting week ending September 15, 1997.

^{3/} See 47 FR 44705 (October 12, 1982).

is difficult to project reliably the extent to which reserves in excess of applied vault cash will be required by these institutions.

The Board therefore is requesting comment on a proposal to amend Regulation D to return to a system of lagged reserve requirements. Under the proposal, a lag of thirty days (two full maintenance periods) would be introduced between the beginning of a reserve computation period and the beginning of the maintenance period during which reserves for that computation period must be maintained. The reserve maintenance period therefore would not begin until seventeen days after the end of the computation period. The proposal also provides for a two-period lag in the computation of the vault cash to be applied to satisfy reserve requirements.^{4/} Providing a two-period lag for both required reserves and applied vault cash will allow the Federal Reserve, as well as the depository institutions, to calculate the level of required reserve balances before the beginning of the maintenance period. The increased lag also should reduce the level of resources that depository institutions and the Federal Reserve currently must devote to estimating and projecting required reserve balances.

The Board's proposal will not affect the provisions of Regulation D concerning the carryover of excess or deficiencies in a depository institution's reserve account.

^{4/} Applied vault cash for an individual institution is equal to the lesser of total vault cash or required reserves.

The Board proposes to implement the shift to a lagged reserve requirement in July 1998. The Board believes that the transition to the new system could be made most easily after completion of the changeover of software used by the Federal Reserve to process most data flows, currently projected for March 1998, and prior to the annual deposit panel shifts that will take place in September 1998.

Initial Regulatory Flexibility Analysis

The Regulatory Flexibility Act (5 U.S.C. 601-612) requires an agency to publish an initial regulatory flexibility analysis with any notice of proposed rulemaking. An initial regulatory flexibility analysis must include: (1) a description of the reasons why action by the agency is being considered; (2) a statement of the objectives of, and legal basis for, the proposed rule; (3) a description of and, where feasible, an estimate of the number of small entities to which the proposed rule will apply; (4) a description of the projected reporting, recordkeeping, and other compliance requirements of the proposed rule; and (5) an identification, to the extent practicable, of all relevant Federal rules that may duplicate, overlap, or conflict with the proposed rules. 5 U.S.C. 603(b)

As discussed above, the Board is considering this action to improve the ability of the Federal Reserve to estimate accurately the need for reserves on a timely basis, with the objective of ensuring greater effectiveness of the Federal Reserve's open market operations. Under section 19 of the Federal Reserve Act , the Board is authorized

to promulgate rules concerning the maintenance of reserves. 12 U.S.C. § 461(c). The Board does not believe that there are any Federal rules that duplicate, overlap, or conflict with the proposed rule.

The proposal will affect only institutions that are weekly deposit reporters, which generally include depository institutions that have total deposits of \$ 75 million or greater, as only these institutions currently are required to maintain reserves on a contemporaneous basis.^{5/} The proposed amendments will not increase reporting or recordkeeping requirements associated with Regulation D for institutions that are weekly reporters, but will significantly simplify compliance with the rule for these institutions. The proposal therefore will not increase regulatory burden on small institutions generally and will reduce regulatory burden for those small institutions that are affected.

List of Subjects in 12 CFR Part 204

Banks, banking, Federal Reserve System, Reporting and recordkeeping requirements.

For the reasons set out in the preamble, the Board proposes to amend part 204 of chapter II of title 12 of the Code of Federal Regulations as follows:

PART 204 -- RESERVE REQUIREMENTS OF DEPOSITORY INSTITUTIONS

(REGULATION D)

^{5/} While weekly reporters that are Edge or Agreement corporations or U.S. branches or agencies of a foreign bank may have deposits of less than \$75 million, the deposits of these entities represent only a portion of the total deposits of the larger organizations to which they belong.

1. The authority citation for part 204 continues to read as follows:

Authority: 12 U.S.C. 248(a), 248(c), 371a, 461, 601, 611, and 3105.

2. In § 204.3, paragraph (c) is revised to read as follows:

§ 204.3 Computation and maintenance.

* * * * *

(c) Computation of required reserves for institutions that report on a weekly basis. (1) Required reserves are computed on the basis of daily average balances of deposits and Eurocurrency liabilities during a 14-day period ending every second Monday (the "computation period"). Reserve requirements are computed by applying the ratios prescribed in § 204.9 to the classes of deposits and Eurocurrency liabilities of the institution. In determining the reserve balance that is required to be maintained with the Federal Reserve, the average daily vault cash held during the computation period is deducted from the amount of the institution's required reserves.

- (2) The reserve balance that is required to be maintained with the Federal

Reserve shall be maintained during a 14-day period (the "maintenance period") that begins on the third Thursday following the end of a given computation period.

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By order of the Board of Governors of the Federal Reserve System,
November 6, 1997.

/signed/

William W. Wiles,
Secretary of the Board.
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